

**Summary of Testimony of
Commissioner Linda Breathitt
Federal Energy Regulatory Commission
Before the
Subcommittee on Energy and Air Quality
Committee on Energy and Commerce
United States House of Representatives**

September 20, 2001

Much of FERC's emphasis in the near future will be to complete the development of Regional Transmission Organizations (RTOs) with clear responsibilities, independence, and sufficient scope. Any departure from the voluntary approach to RTO formation the Commission undertook in Order No. 2000 should be preceded by a formal notice and comment rulemaking in order to give state commissions and other parties the opportunity to participate more fully.

I believe the current voluntary reliability system, which has been in place for over three decades, should be replaced with one in which a self-regulated reliability organization, with oversight by the Commission, enforces mandatory reliability standards. I also believe that interconnection rules should be clarified to ensure that new sources of generation are able to interconnect to the transmission system, and that we carefully consider the associated costs.

I support the repeal of the PUHCA, conditioned upon the grant of enhanced authority to the Commission to address market power problems, and assurance that both FERC and the states would have greater access to the books and records of holding companies. I also support repeal of the mandatory purchase requirements in Section 210 of the PURPA, subject to new provisions that would remove disincentives for renewable generation sources.

I fear that the goal of a national grid may be unattainable absent legislation granting FERC a role in transmission siting. I recommend that FERC be granted Federal eminent domain authority over interstate lines in order to centralize planning, expansion, and siting decisions.

FERC could improve its oversight capabilities with clear authority to collect and publish transactional data, while protecting proprietary information. I also recommend expansion of FERC's authority to remedy violations of law.

Finally, in light of the tragic events of September 11, 2001, the Commission has issued a Policy Statement to assure the industry that we favor the recovery of costs associated with new procedures and facilities to safeguard the electric transmission grid and gas and oil pipelines. Under FERC's dam safety oversight authority, each jurisdictional hydroelectric facility has in place an emergency action plan.

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Mr. Chairman and Members of the Subcommittee:

I appreciate this opportunity to appear before you today to discuss the Federal Energy Regulatory Commission's (FERC) role in developing competitive wholesale power markets and its role in ensuring the continuing development of our Nation's electric power industry. As requested by the Subcommittee, my testimony addresses the following issues: (1) significant changes in the electric power industry; (2) the Public Utility Holding Company Act of 1935 (PUHCA) and the Public Utility Regulatory Policies Act of 1978 (PURPA); (3) the status of Regional Transmission Organization (RTO) formation; (4) FERC's role in the siting of electric transmission facilities; (5) FERC's role in overseeing wholesale electricity markets; (6) FERC's refund authority; and (7) measures undertaken to protect the integrity of the Nation's electric power infrastructure. Where appropriate, my testimony includes comments on legislation that I believe is needed to assist FERC in continuing the development of competitive wholesale markets.

In 1996, with the issuance of Order Nos. 888 and 889, FERC established the foundation for competitive wholesale power markets in the United States. With these rules, FERC ordered all transmission-owning public utilities to file nondiscriminatory open-access tariffs, thereby opening up interstate transmission. FERC's goal was to ensure that customers have the benefits of competitively priced generation.

With the issuance of Order No. 2000 in December 1999, FERC continued its effort to create open and fair competitive markets. Order No. 2000 focused on the formation of Regional Transmission Organizations (RTOs). The Commission found that RTOs may eliminate undue discrimination in transmission services that can occur when the operation of the transmission system remains in the control of vertically-integrated utilities. The Commission also found that RTOs can improve grid reliability, improve market performance, and facilitate lighter-handed regulation. Much of FERC's emphasis in the near future will be to complete the development of RTOs with clear responsibilities, independence, and sufficient scope.

Since the Commission began promoting RTOs as a means to remove barriers and impediments present in wholesale electricity markets, I have been fully committed to the goal of RTO implementation. When the Commission deliberated over how to attain the objective of RTO formation, we decided to adopt an open collaborative process that relied on voluntary regional participation. In a series of orders issued on July 12, 2001,

the Commission dramatically departed from the voluntary approach we pursued in Order No. 2000 by directing the formation of four specific RTOs for the United States, excluding Texas.

I dissented on this aspect of the July 12 orders. My concern was that this decision on RTO formation departed from the basic philosophies embodied in Order No. 2000, and that any such action should be preceded by a formal notice-and-comment rulemaking. This path would allow the Commission to make a reasoned decision informed by the views of all interested parties – most importantly, state commissions.

Apart from the departure from the voluntary nature of Order No. 2000, I have further concerns with July 12 orders' determinations regarding RTO scope and timing. I certainly favor the development of large RTOs reflecting natural markets. I am not, however, convinced that four RTOs would meet the noble goals of Order No. 2000 any better than six or seven -- or even eight -- RTOs of sufficient size. In addition, I believe that the Commission's July 12 decisions demonstrate little regard for the status and timing of RTO formation efforts in various regions of the country. The process of merging markets as RTOs are formed is revealing itself to be a highly technical and complex endeavor. It is my view that the Commission should recognize this in developing realistic expectations.

I also felt it necessary at the time to comment on the majority's assertion that forming larger RTOs will result in lower wholesale prices, and do so now. This is a laudable goal, and as such, I embrace it. However, the promise of lower wholesale electricity prices is one that I, as a federal official, am not willing to make to consumers at this time. Competitive markets should produce lower prices; but we have not yet reached that level of market development. Consequently, I have urged my colleagues to be more circumspect in promising lower prices. Consumers and ratepayers of electricity are going through a trying time at present. We need to be honest and up front as to the benefits and, yes, sometimes the struggles, of moving toward competition.

Of utmost importance in the development of competitive energy markets is reliability. I believe that the voluntary reliability system, which has been in place for over three decades, should be replaced with one in which a self-regulated independent reliability organization, with oversight by the Commission, establishes and enforces mandatory reliability standards. I would support legislation which authorizes a system for assuring the reliability of the electric grid that: (1) is mandatory, (2) requires sanctions and penalties for failure to comply with reliability rules, and (3) is subject to federal oversight. In my view, such a change in the manner in which the reliability of the interconnected grid is overseen and managed is required in order to ensure a competitive bulk power market. I would wholeheartedly support the establishment of a self-regulated independent reliability organization, with oversight by the Commission.

I believe that interconnection rules should be clarified in order to ensure that new sources of generation are able to interconnect to the transmission system. FERC has stated its intent to evaluate in the near future the importance of standardizing interconnection policies and procedures in a generic proceeding. I fully support such standardization. A related issue is who should bear the costs of new interconnections and upgrades. These pricing decisions need to be made carefully and with consideration of the multiple factors at issue. Any changes in cost responsibility for interconnections should be accomplished through a formal rulemaking, where all affected parties have an opportunity to express their views.

There has been significant discussion among industry participants concerning the conditional repeal of both PUHCA and the mandatory purchase requirements of PURPA. If PUHCA is repealed, I urge that such repeal be conditioned upon the grant of enhanced authority to the Commission to address market power problems, and assurance that both the Commission and the states would have greater access to the books and records of holding companies. I also support repeal of the mandatory purchase requirement in Section 210 of PURPA, subject to new provisions that would remove disincentives for renewable generation sources.

Another issue that arises in the context of FERC's goal to encourage competition in wholesale electric markets is the Commission's role in the siting of transmission

facilities. I fear that the goal of a national grid may be unattainable absent a new approach to transmission planning, expansion, and siting. Currently, under the Federal Power Act, the Commission has no role in the permitting and siting of new transmission facilities. I believe that shortages of transmission are no longer just single state issues; instead, these shortages have become interstate commerce issues that must be addressed by the federal government.

There have been proposals to use federal eminent domain as a backstop to a cooperative, regionally-based approach to transmission and siting issues. In essence, FERC would be granted eminent domain authority, which we, in turn, would be allowed to cede to regional regulatory compacts. My primary concern with this approach is that it could result in costly and inefficient duplication of processes, records, and efforts by the various decisional authorities involved in transmission siting. As we have seen with the Commission's hydropower licensing program, for example, it is very difficult to build speed into a process over which several entities exercise jurisdiction. While the Commission has made great progress in streamlining cumbersome processes in this regard, I would caution the Subcommittee about initiating a new regime for transmission siting that could easily be mired in bureaucratic wrangling.

My recommendation would be for FERC to be granted federal eminent domain authority similar to the authority the Commission exercises with respect to the siting of

interstate natural gas pipelines under the Natural Gas Act. The Commission could build into its implementation of such legislation procedures to ensure cooperation by the states and regional input. I believe this more centralized approach is necessary from an efficiency standpoint, and will result in less bureaucracy and more timely decisions for transmission providers and consumers. Furthermore, I am not advocating that the Commission should have siting authority for electric distribution lines or power plants. I believe state governments are best positioned to make those determinations.

I also have a concern that there is not sufficient investment in transmission facilities. In my opinion, the transmission system is not keeping pace with the growing demand in the bulk power market. The difficulty associated with siting is one reason for this. Others are that the industry is increasingly unwilling to make transmission-related investments given the uncertainties that exist in an industry still in the midst of restructuring, as well as the risk of earning inadequate returns on new transmission investments. The Commission must do its part to ensure that its transmission pricing policies incorporate an allowance for reasonable returns on investments. Independent transmission companies as well as merchant transmission companies need certainty to develop their plans.

In order to provide effective oversight of wholesale electricity markets, FERC is preparing itself to operate in today's fast-paced commercial environment. A critical

element of market oversight is the availability of market information in a usable format. There is clearly a relationship between strong market transparency rules and effective regulation. I strongly believe that transparency acts as an effective deterrent to market power by allowing regulators and the public to monitor the marketplace for abuses. The lack of accurate, timely, and easily accessed pricing information can impede competition and liquidity; and for that reason, I have supported many FERC initiatives aimed at expanding the range of publicly available transactional information. With a view toward legislative action, I recommend that FERC and the Energy Information Administration be granted clear authority to collect and publish appropriate transactional data, while protecting proprietary information. These goals are not inconsistent with one another.

The Subcommittee has asked for comment on the authority of the Commission to remedy violations of law. I believe that it would be helpful for the Commission to have some additional authority to prevent the exercise of market power. In my comments to H.R. 1941, "The Electric Refund Fairness Act of 2001," I indicated my support for legislation that would expand the refund authority set forth in section 206(b) of the Federal Power Act. I did, however, emphasize that, in addition to the objective of protecting consumers, I believe it is important for regulators to seek to minimize uncertainty of energy transactions. For example, I would not advocate granting the Commission authority to reopen and order refunds on past transactions. That said, I would welcome legislation amending the FPA to allow the Commission to order refunds

as of the date formal notice of a complaint is issued. All interested persons would be on notice that transactions are the subject of complaint or investigation, and that rates may change and refunds may be ordered as a result. Customers would have the added protection of an earlier refund effective date. I would also advocate lengthening the refund effective period beyond the current fifteen months; I have suggested twenty months after the refund effective date would be appropriate. Both goals of protection and certainty would be met under this framework.

In addition, I believe an amendment to the FPA to give the Commission authority to assess penalties, in addition to refunds and interest, could act as a powerful deterrent against the abuse of market power. However, I believe that, in the interest of certainty, a statutory upper limit to any such penalties should be included. Further, I would suggest that any limits on new penalty authority should be high enough to be effective and withstand the passage of time.

Finally, in light of the tragic events of September 11, 2001, the Subcommittee has asked for comment on the security of the Nation's energy infrastructures. FERC's role in the security of the energy transportation and supply infrastructure is very limited. However, the Commission's dam safety program extends to every jurisdictional hydroelectric facility, and each has in place an emergency action plan. In the event of

emergency, these plans trigger procedures designed to minimize the impact of a breach on downstream property and homeowners. While jurisdictional pipelines and transmission owners are subject to certain reporting requirements, FERC does not have the authority to prescribe or monitor pipeline and electric transmission security. However, our staff is in contact with pipeline and transmission companies, many of which are operating under heightened security procedures.

The Commission's regulatory purview is largely economic; and in this regard, we recognize that the entities under FERC's jurisdiction may incur extraordinary expenses as a result of the terrorist attacks that have taken place. In particular, electric, gas, and oil companies have begun to adopt new procedures and install new facilities to further safeguard the electric power transmission grid and gas and oil pipeline systems. The costs of such additional security measures remain unclear. In order to reduce the uncertainty about company's ability to recover expenses, the Commission issued a Statement of Policy on September 14, 2001, to assure the industry that our policy favors recovery of such costs.

In closing, I emphasize that comprehensive federal electric legislation is needed to address important and unresolved issues in the restructuring of the electric industry. The Commission must have sufficient authority to advance its goals of achieving fair, open

and competitive bulk power markets. Current impediments to the development of such markets must be removed as quickly as possible so that the intended benefits of restructuring for the American consumer ultimately may be realized.